

EXHIBIT 7

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Themselves and All Others Similarly Situated

SUPERIOR COURT OF CALIFORNIA

FOR THE COUNTY OF SAN DIEGO

KARON AND L.B. CHIP EDLESON,
On Behalf of Themselves and All Others
Similarly Situated,

Plaintiffs,

v.

AMERICAN HOME SHIELD OF
CALIFORNIA, INC.; AMERICAN HOME
SHIELD CORPORATION;
THE SERVICEMASTER COMPANY; and
DOES 1 through 20,

Defendants.

) Case No. 37-2007-00071725-CU-BT-CTL

) MEMORANDUM OF POINTS AND
) AUTHORITIES IN SUPPORT OF
) PLAINTIFFS' MOTION FOR A
) PRELIMINARY INJUNCTION

) CONDITIONALLY UNDER SEAL
) PURSUANT TO CRC 2.551(c)

) (The enclosed record is subject to a motion or
) application to file the record under seal)

) Dept: 70

) Judge: Hon. Jay M. Bloom

) Date: November 30, 2009

) Time: 11:00 a.m.

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1 **I. INTRODUCTION**

2
3 Even after two years of litigation and a failed settlement that contemplated that AHS would
4 mend its ways, AHS continues to engage in egregious, systematic, and wrongful business practices
5 that deny homeowners the benefits of the home warranty plans purchased from AHS. A preliminary
6 injunction should be issued because the overwhelming evidence presented herein amply
7 demonstrates that plaintiffs have a reasonable probability of success on the merits and that Class
8 Members are being irreparably damaged due to AHS's false advertising and unfair business
9 practices.

10 AHS falsely advertises that it "can help make covered repairs or replacement easier and less
11 costly" for consumers who purchase its home warranty plans. In order to convince consumers to
12 purchase an AHS plan, AHS states that it "is committed to and solely focused on providing relief
13 from home repair hassles," and "[i]f AHS determines your covered system component or appliance
14 can't be repaired by a service contractor, it will be replaced."

15 These advertisements are false since AHS fails to disclose that it trains its contractors to
16 "Think Denial," to repair rather than replace items, and to charge consumers substantial sums of
17 money for items covered under the warranty plans under false pretexts. AHS also fails to disclose
18 that the contractors it hires to perform repairs for consumers under its home warranty plans sign
19 uniform, fixed-rate contracts with AHS that would result in substantial and recurring losses to the
20 contractors *if* the sole source of the contractors payment was AHS. If this were the case, of course,
21 no contractor would work for AHS. However, AHS encourages its contractors to make a profit not
22 from AHS, but from the very consumers for whom AHS is allegedly providing "protection" from
23 such charges. AHS does so by training and financially incentivizing the contractors to wrongfully
24 deny claims based on pre-textual reasons such as "lack of maintenance" and "improper installation."
25 Once the claim is wrongfully denied, AHS pays zero and the contractor is free to charge the
26 consumer whatever it wants to repair or replace the item since it is not covered by the home warranty
27 plan. Indeed, as Exhibit B amply demonstrates, a consumer with an AHS home warranty plan is far
28 worse off than a consumer without one since the AHS customer ends up paying up to eight times

1 what a normal consumer has to pay to fix or replace something because they have to pay the full
 2 retail rate in addition to the cost of the AHS home warranty plan and the service fee imposed by the
 3 contractor. Since AHS never has any intention of honoring the terms of its home warranty plans, it
 4 is engaging in promissory fraud.

5 Of course, AHS never tells its customers about its nefarious relationship with the contractors.
 6 Instead, it attempts to scare consumers into buying its worthless home warranty plans by including in
 7 its advertisements the average costs that consumers not covered by a home warranty plan pay to
 8 have things repaired and replaced. This, of course, along with AHS's other false advertisements and
 9 assurances, falsely misleads the consumer to believe that AHS will actually fix or replace things
 10 covered under its home warranty plans. If AHS revealed the rock bottom flat-rate pricing
 11 agreements it enters into with its contractors, no consumer would ever buy an AHS home warranty
 12 plan. *See Ex. A* (demonstrating that AHS pays its contractors as little as 14% of what it actually
 13 costs to do the job). Indeed, even for the rare AHS customer who does not get gouged by AHS's
 14 complicit contractors, AHS customers pay between 34-72% of the flat-rate payment AHS's
 15 contractors receive since they have to pay a service fee for each call. *See Ex. C.*¹ Finally, AHS
 16 continues to violate Ins. Code §790.3 (which requires AHS to "conduct and diligently pursue a
 17 thorough, fair, and objective investigation" of its customers' claims) since it does nothing to
 18 investigate Class Members' claims and instead relies exclusively on its third party contractors, who
 19 are trained to "Think Denial" and gouge the Class Member.

20 **II. SUMMARY OF EVIDENCE**

21 AHS violates the law by:

22
 23 [W]rongfully denying legitimate warranty claims covered by the
 24 policies, setting guidelines and stipulations which penalize contractors
 25 for expending resources to resolve problems covered under the
 26 policies thereby inducing contractors to fraudulently represent to
 policyholders that legitimate claims are not covered under the policy,

27 ¹ Indeed, AHS's fraud is amply demonstrated by the fact that AHS would go bankrupt if it honored the terms of its home
 28 warranty plans and actually paid contractors the market rates necessary, according to AHS's own survey, to properly fix
 the systems covered under AHS's home warranty plans. *See Ex. D.*

1 through bogus denials, band-aid repairs, and gouging consumers with outrageous non-covered
2 charges. *See* Weaver Dec. at Exs. 17 – 18, 26 – 51.

3 AHS, on the other hand, will suffer no legitimate hardship if the injunction is granted.
4 Detailed below, Plaintiffs' requested relief simply seeks to have AHS honor the terms of its home
5 warranty plans and merely conditions AHS's "continued activity on compliance with California's
6 consumer protection laws." *People v. Mergent, Inc.*, 170 Cal.App.4th 333, 341 (2009) (explaining
7 that trial court was well within its "broad discretion" to enjoin defendant from conducting any
8 business in California without complying with California's consumer protection laws).

9 **D. Plaintiff's Requested Relief**

10 This Court's power to enjoin AHS's business practices is "extraordinarily broad."
11 *Consumers Union of U.S., Inc. v. Alta-Dena Certified Dairy*, 4 Cal.App.4th 963, 972 (1992). In fact,
12 "because false advertising and unfair business practices can take many forms, the Legislature has
13 given the courts the power to fashion remedies to prevent their 'use or employment' in whatever
14 context they may occur." *Id.* An injunction under California's consumer protection statutes may be
15 prohibitory or mandatory, and may include whatever orders are necessary to prevent the unfair
16 practices from continuing in the future. *Id.* at 972-73. While "it would be impossible to draft in
17 advance detailed plans and specifications of all acts and conduct to be prohibited, since unfair or
18 fraudulent business practices may run the gamut of human ingenuity and chicanery," *Mosk v.*
19 *National Research Co. of Calif.*, 201 Cal.App.2d 765, 772 (1962), the Court should, at a minimum,
20 fashion a remedy that will significantly deter AHS from continuing to engage in its unfair business
21 practices pending trial. Toward this end, Plaintiff requests that the Court order AHS to adopt and
22 implement one of the following remedies, either individually, collectively, or in any combination,
23 within 45 days from the date of the Court's order:

24 **1. Disclose flat rate prices and ranking system to customers**

25 Requiring a defendant to disclose its unlawful business practices is a common type of
26 injunctive relief. *See Colgan*, 135 Cal.App.4th at 677 (trial court issued an injunction requiring
27 defendant "to disseminate on its Web site for a period of six month and in newspapers circulated
28

1 throughout California for a period of 12 consecutive weeks a 'corrective announcement'" that its
2 product was not made in the U.S.A. as defendant falsely claimed); *Consumers Union*, 4 Cal.App.4th
3 at 971 (affirming trial court's injunction requiring dairy company to disclose true health effects its
4 advertisements and on its milk bottles).

5 Here, the Court should require AHS to disclose to its current and potential customers, in its
6 contracts, on its website, via letter, and as part of its marketing materials, that AHS pays its
7 contractors far less than what those contractors would make on a non-home warranty claim. AHS
8 should also disclose that it ranks its contractors primarily based on their average cost per invoice and
9 determines the amount of work a contractor receives based on that ranking. Only then can a
10 consumer fairly evaluate the actual benefits of purchasing or renewing an AHS home warranty plan.

11
12 ***2. Order AHS to stop entering into contractor service agreements that incentivize***
13 ***contractors to deny claims, perform band-aid repairs, up-sell non-covered***
14 ***charges and penalize contractors for performing necessary replacements***

15 As discussed above, AHS enters into operations agreements with its preferred contractors
16 requiring AHS to assign an increased percentage of work to the preferred contractors. Because these
17 contracts require the preferred contractors to keep costs at or below the group average cost per
18 invoice, which is already well below the going market rate, AHS's contractors have a strong
19 financial incentive to deny claims, perform band-aid fixes and up-sell non-covered charges. The
20 contracts also punish AHS's contractors for performing necessary replacements, thus causing them
21 to almost exclusively repair items. Accordingly, the Court should enjoin AHS from entering into
22 any future service agreements that prevent a contractor from earning a profit from AHS and thus
23 force the contractor to charge the consumer for alleged non-covered items in order to be able to
24 make enough money to perform the necessary repair or replacement.
25
26
27
28

1 **3. Require AHS to collect and maintain information regarding the amount of non-**
 2 **covered expenses charged to its customers by its contractors**

3 The Court should order AHS to require contractors to submit to AHS the amounts AHS's
 4 customers are charged by the contractors for non-covered services and upgrades and to ensure that
 5 any such charges are legitimate and reasonable.¹²

6 **E. The Court Should Require Plaintiffs To Post A Bond In A Minimal**
 7 **Amount**

8 Upon entry of a preliminary injunction, a court must require the party seeking the injunction
 9 to produce either an undertaking or put up a bond in lieu of one. C.C.P. §§ 529(a), 995.710. In
 10 determining the amount of the injunction, the trial court "is to estimate the harmful effect which the
 11 injunction is likely to have on the restrained party, and to set the undertaking at that sum." *ABBA*
 12 *Rubber Company v. Seaquist*, 235 Cal.App.3d 1, 14 (1992). "That estimation is an exercise of the
 13 trial court's sound discretion." *Id.* The amount of the undertaking has to be an approximation of the
 14 reasonably foreseeable damages caused by the injunction. *Id.* The defendant bears the burden of
 15 presenting admissible and quantitative evidence of the harm that an injunction would cause.
 16 *Hummell v. Republic Fed. Sav. & Loan Assn'n*, 133 Cal.App.3d 49, 51 (1982).

17 The amount of the undertaking here should be minimal because AHS will not reasonably
 18 suffer any damage if the requested relief is granted. Indeed, Plaintiffs' proposed injunction does not
 19 put AHS out of business, prevent it from selling home warranties, bar any truthful advertising, or
 20 even preclude it from denying any claims that are legitimately not covered by the terms of its
 21 policies.¹³ Instead, the proposed injunction merely requires AHS to deal with its customers in an
 22 honest and truthful fashion. Thus only a de minimus bond should be required.

23
 24
 25
 26 ¹² AHS currently keeps no data regarding how much its contractors charge its consumers, nor does AHS make any effort
 to ensure that such charges are appropriate or reasonable.

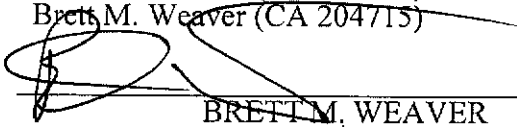
27 ¹³ Amazingly, AHS's "person most knowledgeable" recently testified that such information was "fluff data" and no
 28 interested to AHS. See Sanderson Depo, attached at Weaver Decl., Ex. 21.

1 **IV. CONCLUSION**

2 For the reasons stated above, Plaintiffs respectfully request that the Court grant their motion
3 for preliminary injunction.

4 DATED: October 9, 2009

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